

**NORTH AMERICAN FREE TRADE AGREEMENT (NAFTA)
TECHNICAL INFORMATION FOR PRE-ASSESSMENT SURVEY (TIPS)**

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PART 1. BACKGROUND

1.1 OVERVIEW

On December 17, 1992, President Bush of the United States, President Salinas of Mexico and Prime Minister Mulroney of Canada entered into the North American Free Trade Agreement (NAFTA).

Public Law 103-182 (H.R. 3450); December 8, 1993 (107 STAT 2057) approved the North America Free Trade Agreement that was entered into by the United States, Canada and Mexico (the "Parties"); and the statement of administrative action to implement the Agreement. The NAFTA entered into force on January 1, 1994.

The NAFTA creates a free trade area consistent with Article XXIV of the General Agreement on Tariffs and Trade (GATT) in which tariff and non-tariff barriers to trade are substantially reduced between the Parties. (NAFTA Article 101)

Trade between the U.S. and its two NAFTA partners account for one third of all U.S. international trade. The U.S. – Canada is the largest trading relationship between any two countries in the world. Recent trade statistics show that trade between the NAFTA Parties is valued at \$1.8 billion per day with 62% of that trade conducted under the NAFTA.

1.2 AUTHORITY TO CONDUCT AUDITS

Under 19 U.S.C. 1509 the U.S. Customs and Border Protection may examine records to ascertain the correctness of any entry for determining the liability of any person for duties, taxes or fees which may be due the United States or for ensuring compliance with the laws of the United States administered by the U.S. Customs and Border Protection.

Any person who imported or knowingly caused the importation of merchandise into the customs territory of the United States, exported merchandise, or knowingly caused the exportation of merchandise to a NAFTA country; must provide the records required by law or regulation to the U.S. U.S. Customs and Border Protection within a reasonable time after demand. (See 19 U.S.C. 1509(a)(2)(A)(ii))

1.3 RISK MANAGEMENT

Customs performs its duty in an environment where decisions regarding the allocation of finite resources have become increasingly important. We define risk as the degree of exposure to the chance of non-compliance that would result in loss to the trade, industry or public. Risk management is the integrated process for identifying and managing risk in trade compliance.

1.4 OBJECTIVE

Provide guidance in performing a Pre-Assessment Survey (PAS) of the importer's internal controls for the North American Free Trade Agreement (NAFTA) and evaluating the results.

Note: The evaluation of the importer's internal controls for NAFTA is limited to a determination as to whether the Certificates of Origin as maintained by the importer are timely, accurate and sufficient. The importer's internal controls for NAFTA should address the records requirements to secure and maintain certificates of origin to support the importer's claims for NAFTA preferential treatment.

The Focused Assessment (FA) process does NOT include determining whether the goods referred to in the Certificates of Origin that are held by the importer actually qualify as originating goods under the

NAFTA. Determinations on the origination of the goods and their resulting eligibility for NAFTA preference are made exclusively through the NAFTA verification process.

The NAFTA evaluation should be limited to a determination as to whether the Certificates of Origin as maintained by the importer are accurate and support the NAFTA status of the imported goods. Unlike GSP where a question regarding content would result in a request from the exporter for supporting documents, under NAFTA supporting documents are not to be requested. However, where there is a question of origin or content, consideration should be made as to whether a referral should be prepared for follow-up by a NAFTA verification either through a port-initiated verification or a Joint Verification Team (JVT).

1.5 LEGAL AND REGULATORY PROVISIONS AND REFERENCES

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal controls to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and the terms in this technical information guide are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and the American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

Chapter 3 of the NAFTA provides for preferential treatment for originating goods imported from another Party. A good is considered originating if it meets all of the requirements of the NAFTA Chapter 4 rules of origin. Customs procedures concerning claims for preferential treatment for originating goods are set out in Chapter 5 of the Agreement.

The Chapter 4 Rules of Origin are implemented by the Uniform Rules of Origin Regulations (Part 181, App. of the U.S. Customs Regulations [19 CFR 181.131]) and General Note 12 of the Harmonized Tariff Schedule of the United States for imports into the United States. The Uniform Rules of Origin Regulations are trilateral regulations that have been incorporated into the domestic regulations of each of the Parties.

Customs Procedures of Chapter 5 of the NAFTA are implemented in the U.S. by Part 181 of the Customs Regulations (19 CFR 181.1 through 181.122).

The Rules of Origin provided in Part 102 of the Customs Regulations are for the specific purposes of determining the country of origin for goods of NAFTA Parties. Determination of the country of origin is necessary for proper marking of the good and application of the correct staged rate of duty if the duty rate has not been phased out to zero. The rules of origin of Part 102 are not used to determine the originating status of goods.

General definitions applicable to the NAFTA are found in Chapter 2 of the Agreement and in Section 2 of the Rules of Origin Regulations (Part 181, App. of the U.S. Customs Regulations [19 CFR 181.131]). Definitions that are specific to a Chapter, Article or Annex of the Agreement are found at the end of the Chapter, Article or Annex.

PART 2. PROGRAM GUIDANCE

2.1 CLAIMS FOR NAFTA PREFERENTIAL TREATMENT

To claim NAFTA preferential treatment for imported goods the importer must:

1. Make a written declaration based on a valid certificate of origin (Art. 502 NAFTA; 19 CFR 181.21)
 - A written declaration may be made by entering the prefix "CA" or "MX" with the tariff number of originating goods on the CF 7501 entry summary

- Or at any time within one year of the date of importation using the provisions of 19 USC 1520(d)
 - When the importer makes a claim for preferential treatment, NAFTA originating goods are entitled to the duty rate in the "special" column that is indicated "CA" or "MX"
 - The merchandise processing fee is also waived for NAFTA qualifying merchandise
2. Possess a valid certificate of origin (CO) at the time of the declaration (Art. 502 NAFTA; 19 CFR 181.21; CD No. 3810-014, June 28, 1999)
- A valid CO:
 - ✓ Has the signature of the exporter or an authorized agent
 - ✓ Is dated and the date of execution is prior to the date of the NAFTA claim
 - ✓ Is in English or the language of the exporting Party (If in Spanish or French, the importer must provide a translation on request from USCS)
 - ✓ Is on Customs Form 434 or an approved alternative
 - A valid CO is required for each importation
 - Description provided on the CO is sufficient to allow an import specialist to identify the goods
 - A CO may be applicable to:
 - ✓ A single importation
 - ✓ Multiple importations of identical goods within a specified period up to one year (Blanket CO)
 - A CO is valid for 4 years from the date of signature
 - Policy Guidelines for the use of the NAFTA CO are established by Customs Directive No. 3810-014, dated June 28, 1999
 - ✓ A CO is valid provided that it is properly completed, signed and dated
 - ✓ If the importer did not possess a valid CO at the time the claim was made, the claim will be denied
 - ✓ A CO that contains inadequate information, is unsigned or is otherwise defective on its face is invalid
 - CO's that are "Otherwise defective" include those with: incorrect classifications, inadequate descriptions, missing date, wrong blanket period
 - The importer will be allowed at least 5 working days to submit a corrected CO
3. Maintain documentation in the United States, including the certificate of origin, relating to the importation of the good. (19 USC 1508, Art. 502 NAFTA; 19 CFR 181.22)
- Importer must maintain the CO for a period of 5 years from the date of importation
4. Provide the certificate of origin to Customs on request (19 USC 1509, Art. 502 NAFTA; 19 CFR 181.22)
5. Promptly make a corrected declaration when warranted (19 USC 1508, Art. 502 NAFTA; 19 CFR 181.22)

2.2 EXAMPLES OF RED FLAGS

The examples provided below may serve as indicators that there are potential compliance problems with the NAFTA claims being submitted by the importer.

Care must be exercised by the auditor to properly identify issues that are compliance problems with the importer's claims vs. the eligibility of the goods to qualify for preferential treatment because they originate in the NAFTA territory. Originating status of the goods can only be verified through the exporter using the NAFTA verification procedure.

The importer is not responsible to maintain documentation that will support the origination of the goods that is certified by the exporter on the NAFTA CO. A request from Customs for information to support the exporter's declaration on the CO will trigger a NAFTA verification and require the procedures that are formalized in the Agreement and the issuance of a determination.

Requesting information about the good from the importer for determining classification, value or admissibility; asking for the NAFTA CO; or asking the importer questions about the NAFTA claim that the importer would have direct knowledge does NOT trigger a verification. The importer may also voluntarily provide information furnished by the exporter or producer in accordance with 19 CFR 181.72(c).

While conducting a FA review the auditor may develop some information that would raise some "red flags" concerning the goods and whether they qualify as originating. These questions can only be addressed through the NAFTA verification process and the auditor should consider making a referral for verification to be conducted by an import specialist or a joint verification team.

The list of "red flags" below are divided into two categories: those listed in category (1) are conditions that may indicate a potential problem that can probably be addressed directly with the importer without the need for information that would be available only from the exporter or producer; the "red flags" listed in category (2) are more likely to necessitate exporter involvement and may need to be addressed outside of an FA; in these cases a referral for a NAFTA verification may be warranted.

A. CATEGORY (1) Red Flags:

- Importer has insufficiently documented, poorly defined, or no internal controls for accurately declaring NAFTA preferences for Customs purposes. Examples:
 - ✓ Importer does not monitor or interact with the broker on NAFTA eligibility issues
 - ✓ Importer relies on one employee to handle NAFTA compliance, and there are poor or no management checks or balances over this employee
 - ✓ Importer Customs staff lacks knowledge of NAFTA eligibility rules and requirements
- Importer offers unreasonable explanations to Customs
- Previous negative determinations, denials or failed verifications on the same merchandise being imported from the same supplier (Is there documentation that indicates that the importer was notified of production changes so that the good now qualifies? If not, is the importer reasonable in his reliance on the CO?)
- Importer fails to cooperate or respond to Customs
- Importer has high turnover of people in key positions
- There is significant variance between the importer's data and Customs data
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with NAFTA claims (e.g., classification problems, inventory control problems for fungible goods, invalid or improperly completed certificates of origin, lacking a certificate of origin for a claim, reporting incorrect country of origin)
- One importer representative dominates NAFTA preference claims procedures and record keeping without monitoring or management oversight
- There is a large number of NAFTA Manufacturer Identifications (MIDs)
- There is a large quantity of NAFTA merchandise over many HTSUS numbers
- There is no monitoring of the classification procedure or records process that serve as the basis for the NAFTA preference claims
- There is a sharp increase of NAFTA imports from a prior period.
- The importer and the NAFTA producer are related
- The importer's reliance on the information certified in the certificate of origin is not reasonable (May be indicated if there are imports of NAFTA merchandise for which the exporting country is an unlikely source)

- Specific issues are identified in the profile
- Importer did not request, maintain, or review Certificates of Origin (Customs form 434) supporting the qualification of merchandise for NAFTA preferential treatment
- The CO is incorrectly prepared i.e. the HTS information is not correct but can be corrected within the requirements of 19 CFR 181.22.
- The blanket CO is signed subsequent to the beginning of the blanket period claimed and the importer has declared NAFTA for imports of the good prior to the signed date.
- Patterns of “type 02” entries and entries with NAFTA claims vary inversely. For example, the merchandise that was previously subject to quotas was subsequently being claimed as NAFTA eligible and not subject to quota restrictions.
- There are significant shifts in importing practices and claims; for example:
 - ✓ Shifts from claims for benefits of HTSUS 9802 to claims for NAFTA preference
 - ✓ A sudden rise in NAFTA claims and corresponding decline in tariff preference level (TPL) claims
- The importer does not clearly differentiate or does not demonstrate an understanding of 9802 benefits vs. preference claims under NAFTA
- There are changes in classifications from one time frame to another for a considerable portion of an importer’s imports (This may be especially significant if any of the merchandise is subject to quota or dumping/countervailing duties from non-NAFTA countries; or if there is a shift away from HTSUS numbers that are associated with complex rules of origin or require RVC calculations.)

B. CATEGORY (2) Red Flags:

(Conditions that may be more appropriately addressed outside of the FA process and may warrant referral for a NAFTA verification)

- There are imports from a specific exporter or under an HTSUS number or country of origin that have been identified by Customs because of known or suspected NAFTA problems
- There are imports of NAFTA merchandise for which the exporting country is an unlikely source
- There are no prior verifications of NAFTA exports from the importer's principal NAFTA suppliers
- There are imports of merchandise where the specific rule of origin provided in HTSUS General Note 12 is very restrictive, complicated, or difficult to meet
- There are imports of merchandise where the applicable specific rule of origin has specific requirements, or requires that certain components originate
- The alternate Normal Trade Relations (NTR) duty rate for the merchandise imported is relatively very high
- There are restrictions imposed on imports of the merchandise from other countries, but not from the NAFTA Parties (e.g. dumping or countervailing duties, visa requirements, quota restrictions, trade sanctions).
- The exporter preparing the CO is not the producer of the good but rather a middleman or warehouse.
- The compliance measurement discrepancy rates are high for HTSUS numbers that importer frequently uses regarding NAFTA; or there are no verifications of the HTSUS numbers
- There are imports from a specific exporter or under an HTSUS number or country of origin that have been identified by Customs because of known or suspected NAFTA problems

2.3 EXAMPLES OF BEST PRACTICES

(Applicable only to the Importer filing claims for NAFTA preference.)

- The importer’s Internal controls over NAFTA claims:

- ✓ Are in writing,
- ✓ Include procedures for monitoring and feedback, and
- ✓ Are monitored by management
- One manager is ultimately responsible for control of the Import Department, including NAFTA eligible merchandise. That manager has knowledge of Customs matters and the power to ensure that internal control procedures for imports are established and followed by all importer departments
- Written internal control procedures assign NAFTA duties and tasks to a position rather than a person
- Importer has good interdepartmental communication about NAFTA matters
- Importer conducts and documents periodic reviews of NAFTA, and uses the results to make corrections past and present to entries and changes to its import operations as appropriate
- Suppliers, as well as other departments within the importer's organization such as engineering and purchasing, provide sufficient descriptions of merchandise to the import department to permit accurate classification and resulting determination of NAFTA eligibility
- The importer's internal controls contain prudent business practices (such as designating the material supplier for the NAFTA goods) that are meant to ensure that the importer can reasonably rely on certifications provided by the exporter. E.g. Because of product liability and business arrangements many auto parts producers are required to use customer approved material suppliers)
- The importer's internal controls involve a verification process to determine that the imported merchandise qualifies for NAFTA
- The importer has procedures to obtain certificates of origin from all NAFTA suppliers prior to the initial import date of any of the merchandise covered by the CO
- Internal controls ensure that the CO and related documents are maintained by the importer for the five year required period
- Importer has procedures in place to furnish Customs copies of applicable certificates of origin when requested
- Importer maintains a NAFTA database or listing of imported merchandise that would readily identify transactions that claim NAFTA preference
- The importer (or the importer's agent) visits the plant in the NAFTA country where the products are produced
- The importer performs an annual review of specific rules of origin (General Note 12 of the HTSUSA) that apply to imported merchandise to remain current with any changes to NAFTA requirements.
- The Importer communicates regularly with the filer to keep the filer's information current on what merchandise is NAFTA eligible and which is not.

2.4 EXAMPLES OF DOCUMENTS AND INFORMATION TO REVIEW

- Internal control policies and procedures used to ensure the validity of NAFTA certificates of origin; they should assure that:
 - ✓ Valid CO's are in importer's possession prior to making NAFTA claim
 - ✓ CO's are signed and dated prior to date of importation
 - ✓ CO's pertain (HTS # and description match) to the merchandise imported and claimed for NAFTA
 - ✓ CO's cover each importation on which NAFTA preference was claimed
- Importer's response to the questionnaire
- Interviews with importer staff concerning general internal controls and internal controls specific to NAFTA claims
- Importer's documentation that supports monitoring and verification of established and/or written internal controls for NAFTA, including:
 - ✓ Communications between the person responsible for monitoring NAFTA eligibility and the entry filer
 - ✓ Binding rulings concerning NAFTA eligibility

- ✓ Classification rulings for NAFTA merchandise
- ✓ Invoices, specification sheets, or other documents providing detailed descriptions of NAFTA merchandise
- ✓ Lists containing NAFTA part numbers, descriptions, quantities imported, and unit costs
- ✓ Bills of lading or other evidence of direct transport to the United States
- ✓ Previous positive determinations for the same merchandise
- ✓ Communications between the importer and the exporter concerning NAFTA eligibility of the merchandise.

PART 3. RISK AND INTERNAL CONTROL GUIDANCE

PAS team judgment should be used to determine the type and amount of testing needed to evaluate the effectiveness of internal controls and to determine if there is a sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) phase.

Using the chart and guidelines below, determine through limited judgmental testing whether the importer’s internal controls are effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. The **risk exposure**, and
2. The **internal control** system by determining if the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

3.1 RISK

A. Preliminary Assessment of Risk

Before any audit work begins at the company the team should make a preliminary assessment of risk (PAR) using information obtained from Customs or publicly available information. The purpose of the PAR is to evaluate identified potential risks to Customs based on analytical reviews of Customs data and other Customs information. This review will identify areas of potential risk and eliminate some areas with insignificant risk. The PAR should be conducted using the form in Attachment 1 to the PAS Audit Program.

B. Evaluation of Risk Acceptability

After the audit work begins with the company the team will refine the assessment of risk. After all audit work has been completed the team will determine whether risk is acceptable or unacceptable using the PAS Audit Program as summarized in the following steps.

- Determine what activities pose a significant risk to Customs.
- Test the existence, effectiveness and implementation of internal control and determine if internal control is adequate to control risk.
- Using the results of the internal control review, develop and opinion whether risk is acceptable or unacceptable.

3.2 INTERNAL CONTROL

To evaluate the internal control system:

1. Consider the five components of internal control:

- Control Environment
 - Risk Assessment
 - Control Activities
 - Information and Communication
 - Monitoring
2. Review relevant Customs and importer documents to identify and understand relevant internal controls over NAFTA. (Examples of documents and information to review are listed above.)
 3. Determine whether the importer has established and follows procedures. Review:
 - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
 - Documentary evidence (such as a log) of communication with the broker and importer departments on NAFTA issues, including Importer testing of broker operations and verification that the broker followed importer instructions.
 - Importer-specific NAFTA rulings requested. Determine if they are followed.
 - Documentary evidence of internal communications, to ensure that correct information is provided to Customs.
 - Training records and materials relating to NAFTA used to educate staff on Customs matters.
 4. Review written policies and procedures and interview applicable importer personnel to complete appropriate sections of the “Worksheet for Evaluating Internal Control (WEIC) - NAFTA.”

Note: The internal control assessment should include steps to:

- Identify and understand internal controls
- Determine what is already known about control effectiveness
- Assess the adequacy of internal control design
- Determine whether controls are implemented and effective
- Determine whether transaction processes are documented

3.3 EXTENSIVENESS OF AUDIT SAMPLE TESTS (TESTING LIMIT)

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the total NAFTA level that will be reported on. For example, the importer may import from several NAFTA suppliers, but testing may be necessary only for certain companies or only for certain imports that have been identified as the primary risks.

Extensiveness of Audit Tests

PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit
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PAR Level	+	Preliminary Review/ Internal Control	=	Extensiveness of Audit Test	Testing Limit
High		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
Moderate		Weak Adequate Strong		Moderate to High Moderate Low	5-15
Low		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits*.
Column titled "Testing Limit" reflects Customs test sizes.

3.4 EVALUATION OF PRE-ASSESSMENT SURVEY TESTING RESULTS

The following steps are guidance for determining the effectiveness of importer's internal control over NAFTA claims.

1. Complete the "Worksheet for Evaluating Internal Control (WEIC) - NAFTA" to determine whether risk determination is acceptable or unacceptable and document why. Put results of NAFTA testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

Customs considers risk unacceptable when testing reveals that internal controls were not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT:

Do not proceed to ACT if:

- Cost-benefit analysis warrants no further effort, (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant.) and
- The result of review indicated that the error was due to an isolated incident.
- If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

Proceed to ACT if:

- The company does not have an adequate internal control and the review indicated a material loss of revenue that cannot be quantified without statistical sampling or further review.
- The importer will not quantify the loss of revenue.
- The company refuses to take corrective action on systemic errors and it is necessary to calculate a compliance rate to evidence significant non-compliance.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be performed quickly and without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

3.5 EXAMPLES

The following examples of scenarios that may be encountered under PAS are provided for clarification purposes only.

Note: Where there are multiple importations of the same merchandise from the same exporter, the importer will most often utilize a blanket CO issued by the exporter to cover imports for a period of one year. The time period where the risk is highest that the importer will not be in possession of a valid CO when claims are made is early in the blanket period or the beginning of the fiscal year.

Example A: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims were supported by valid certificates of origin in the importer's possession except for one item that was imported on multiple entries throughout the year.

The importer imports multiple products from the exporter who provided a blanket certificate of origin covering multiple products. One product was not included in any certificate of origin provided by the exporter.

The importer agreed to quantify and pay duties on the merchandise for which there was no valid certificate of origin and to modify his internal controls to assure that a valid certificate is in his possession prior to making a NAFTA claim.

Since there were no other revenue issues and correction was made to avoid future problems, the team does not proceed to ACT for revenue.

Example B: Situation in which the team would not proceed to ACT (Compliance)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims were supported by valid certificates of origin in the importer's possession except for one shipment where the invoices indicated that the country of origin was a non-NAFTA country. The NAFTA producer experienced production problems and obtained goods from its parent manufacturing plant in Sweden to fill one of the importer's orders.

The importer agrees to pay the duties and interest due on the one shipment that was not of NAFTA origin and to modify internal controls to assure that NAFTA eligibility is ascertained prior to making claims based on blanket certificates of origin.

Example C: Situation in which the team would not proceed to ACT (Revenue)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims revealed that two products were consistently misclassified on the certificates of origin and entered under that wrong classification. The correct classification and corresponding rule of origin did not affect the goods originating status and there was, therefore, no revenue impact.

The importer agreed to secure a corrected certificate of origin that was promptly provided by the exporter. The importer also agreed to modify internal controls so that the classification error would not recur.

Example D: Situation in which the team would proceed to ACT (Revenue)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and

testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, tests of NAFTA claims indicated that certificates of origin were on file to support claims for preferential treatment. The importer purchases 4 different models of the product, but only 2 are listed on the CO's provided to the importer by the exporter/producer. Based on the examination of correspondence between the importer and the producer, it is disclosed that the NAFTA producer actually produces 2 of the models in the NAFTA territory and the other 2 are purchased by the exporter from its parent company located outside of the NAFTA territory. Most of the shipments contain units of all 4 models and the importer claimed NAFTA preference on all models.

In this scenario the importer does not have CO's to support the preference claims on 2 models of the product. Furthermore, the importer will not be able to obtain corrected CO's from the exporter to cover all models. Preferential treatment should be denied. There is no determination of origin of the goods made in this type of scenario and no NAFTA verification. There is a denial of the claim because there is no valid CO for the goods. The PAS team proceeds to ACT to quantify revenue loss.

Example E: Situation in which the team would proceed to ACT (Compliance)

The importer has internal controls for NAFTA. The internal controls include:

- ✓ Contractual provisions in which the exporter agrees to provide certificates of origin for NAFTA in a timely manner and that specifically identify the goods that are eligible for NAFTA preferential treatment.
- ✓ Provide for reviews of foreign facilities to verify foreign production in the NAFTA country of production and maintenance of documentary information to support importer reviews and testing of NAFTA eligibility, or other basis to reasonably rely on the exporter's statements of eligibility.

In order to determine the importer's internal control effectiveness, the PAS team evaluated the importer's internal control procedures. Specifically, NAFTA claims are tested and the importer's current inventories are reviewed. A recent shipment is found to contain commingled originating and non-originating goods. Though the origination status for the various goods in the shipment is clearly indicated on the invoices, the importer claimed NAFTA preference on all of the goods in the subject importation.

The importer says that the incident is a one-time occurrence caused by a clerical error and does not want to change internal controls.

The imported goods are used by the U.S. importer as materials for goods that the importer produces and then sells to customers in other NAFTA Parties. The U.S. Company, as the exporter, furnishes NAFTA certificates of origin for the goods that are exported.

Since the importer will not change its internal controls and the level of compliance is unknown, the PAS team proceeds to ACT to determine whether the importer meets the acceptable level of compliance for NAFTA.

In this kind of scenario, NAFTA compliance includes the exported product and the declaration made by the U.S. company on the CO's that it completed for exports to other Parties as well as the import compliance for the goods imported under NAFTA preference and subsequently used as materials. The responsibilities imposed on U.S. importers by 19 USC 1509 are extended to any U.S. exporter who executes a NAFTA certificate of origin. (19 U.S.C. 1509(a)(2)(A)(ii))

If the non-originating goods used as materials in the importer's production affect the origination of the good produced and exported to another NAFTA Party, the declaration made by the U.S. company on the CO's that it completed will be a violation of 19 USC 1509. The Importer/U.S. exporter is subject to the same level of culpability and consequences in this export transaction as it would be for a violation of the same law in an import transaction. Customs also have the same enforcement responsibilities for the violation.

Note: Based on non-compliance in the NAFTA area, the Team will proceed to ACT only when the actionable non-compliance is based solely on the responsibilities of the importer in the NAFTA transactions. For import transactions, the importer's responsibility is to possess and maintain a valid certificate of origin for each claim for NAFTA preference. If the importer is in possession of a valid CO the NAFTA claim CANNOT be denied without a NAFTA verification. There is never a negative determination on the origin of the goods based on the information provided by the importer. A negative determination on the origin of the goods can only be issued as a result of a verification conducted through the exporter. If the importer cannot produce a valid CO when requested to do so, then NAFTA preference will be denied. In this case, there is a denial of NAFTA benefits; however, there is no determination as to whether or not the goods originate.

PART 4. REPORT GUIDANCE

The Focused Assessment (FA) process does NOT determine the eligibility of the goods for NAFTA preferential treatment. Whether or not the goods qualify for NAFTA treatment by meeting the rules of origin requirements is not an issue that is to be addressed in a FA report.

Rather, the FA process examines and reports on the written internal controls that the importer (not the exporter or producer) has implemented relative to the claims for NAFTA preference that are made on its importations.

The following are examples of statements that might appear in the summary of audit results when the internal controls are found to be sufficient:

"ABC has adequate internal controls over its Customs related transactions which provide reasonable assurance that the importer is compliant with the laws and regulations and is an acceptable risk to Customs. The conclusions for each review area are summarized below:

- "North American Free Trade Agreement (NAFTA) – Our review of ABC's internal controls over its NAFTA importations, disclosed that the controls in place appear to be functioning as intended with no significant risk of non-compliance to Customs. However, our review of ABC's internal controls, is not designed to determine the NAFTA eligibility of the goods imported. The eligibility of the goods imported claiming NAFTA preference can only be determined by a NAFTA Verification."

NOTE:

Although a NAFTA “determination” can never be issued based on a focused assessment report, it does not mean that the importer’s claims for NAFTA preference cannot or will not be denied if there are NAFTA claims that cannot be supported by the importer. In order to claim NAFTA preference, the importer must have a valid certificate of origin (CO) at the time the claim is made.

NAFTA preference will be denied:

- If the importer does not have a valid CO that covers the importation and claim for NAFTA preference
 - A valid CO:
 - ✓ Has the signature of the exporter or an authorized agent
 - ✓ Is dated and the date of execution is prior to the date of the NAFTA claim
 - ✓ Is in English or the language of the exporting Party (If in Spanish or French, the importer must provide a translation on request from USCS)
 - ✓ Is on Customs Form 434 or an approved alternative
 - A valid CO is required for each importation
 - Description provided on the CO is sufficient to allow an import specialist to identify the goods
 - A CO may be applicable to:
 - ✓ A single importation
 - ✓ Multiple importations of identical goods within a specified period up to one year (Blanket CO)
 - A CO is valid for 4 years from the date of signature
- If the importer’s CO is invalid on its face and the importer cannot produce a corrected CO
 - Policy Guidelines for the use of the NAFTA CO are established by Customs Directive No. 3810-014, dated June 28, 1999
 - ✓ A CO is valid provided that it is properly completed, signed and dated
 - ✓ If the importer did not possess a valid CO at the time the claim was made, the claim will be denied
 - ✓ A CO that contains inadequate information, is unsigned or is otherwise defective on its face is invalid
 - CO’s that are “Otherwise defective” include those with: incorrect classifications, inadequate descriptions, missing date, wrong blanket period
 - The importer will be allowed at least 5 working days to submit a corrected CO
- In the normal course of reviewing the importer’s books and records, evidence is discovered that their claims for NAFTA preference cannot be supported or there is fraudulent activity on the part of the importer concerning the NAFTA claims

For import transactions, the importer’s responsibility is to possess and maintain a valid certificate of origin for each claim for NAFTA preference. If the importer is in possession of a valid CO the NAFTA claim CANNOT be denied without a NAFTA verification. There is never a negative determination on the origin of the goods based on the information provided by the importer. A negative determination on the origin of the goods can only be issued as a result of a verification conducted through the exporter. If the importer cannot produce a valid CO when requested to do so, then NAFTA preference will be denied.

PART 5. WORKSHEET FOR EVALUATING INTERNAL CONTROL (WEIC) – NAFTA

PURPOSE: To determine whether Transaction Value risk is acceptable.

The completion of this worksheet provides evidence that the five components of internal control: Control Environment, Risk Assessment, Control Activities, Information and Communications, and Monitoring were evaluated.

During this phase of the process, an internal control review will be completed and factors for internal control related to an assessment of Risk Exposure including Internal Control Red Flags, Susceptibility, Management Support and Competent Personnel will be considered. The completion of this worksheet provides evidence that these factors were evaluated.

All answers must be linked to supporting documentation.

OBJECTIVES:

Section 1 - Internal Control Questions	Consolidate information learned about internal control through interviews and document reviews to form a preliminary assessment of internal control before testing. For work paper reference column titled "Is Implementation of Control Supported by Documentation and/or Interviews," confirm that the control is implemented through: <ul style="list-style-type: none"> • Interviews and requesting evidence from the company and • Reviews of documents that provide evidence that the company completed the activity.
Section 2 – Preliminary Internal Control Assessment	Use information consolidated in Section 1 to make a preliminary assessment whether internal control is strong, adequate, weak or nonexistent.
Section 3 - Sample Sizes	Use the Preliminary Assessment of Risk (PAR) Level and the Preliminary Internal Control Assessment to determine the sample size for each sample.
Section 4 - Results of Sample Testing	Use information in Section 4 to record the results of PAS testing to evaluate whether internal control is effective to provide reasonable assurance of compliance.
Section 5 - Risk Opinion	Use information in section 1-4 to record the PAS opinion that risk is acceptable or unacceptable

Section 1- Internal Control Questions

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
1.	Does the company have formally documented internal control to assure the validity of all claims for NAFTA preferences?					
2.	Does management approve written policies and procedures?					
3.	Does the company review and update written policies and procedures periodically?					
4.	Is internal control of certificates of origin periodically tested and results documented? This should include post-entry reviews to verify certificates of origin for all NAFTA claims.)					
5.	If weaknesses were found during internal control testing of certificates of origin by the company, did the company correct internal control procedures and entries when appropriate?					
6.	Do written internal control procedures assign duties for ensuring that NAFTA claims are supported by valid certificates of origin to a position rather than a person?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
7.	Does one individual have authority to ensure that internal control procedures for NAFTA certificates of origin are established and followed for all departments?					
8.	Do personnel responsible for ensuring that valid NAFTA certificates of origin are obtained have adequate knowledge and training in Customs valuation?					
9.	Does the company have adequate interdepartmental communication about Customs NAFTA certificates of origin?					
10.	Does the company have procedures to obtain Customs assistance for NAFTA issues when needed and is advice followed when given (e.g., requesting binding rulings)?					
11.	Does the company identify analyze, and manage risk related to NAFTA certificates of origin?					
12.	Has the company identified any risks related to NAFTA certificates of origin and implemented control mechanisms?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
13.	Do internal controls involve a process to determine if reliance on the exporters' certificate of origin is reasonable?					
14.	Does the company have procedures to link specific certificates of origin to Customs entry numbers?					
15.	Do Purchasing, Engineering, other departments, and suppliers provide adequate descriptive information to the Customs Department and/or broker to ensure proper NAFTA classification and eligibility?					
16.	Does the importer have procedures to obtain certificates of origin to support claims for NAFTA preference?					
17.	Does the importer have procedures to track and replace expiring certificates of origin before they expire?					
18.	Does the importer maintain a NAFTA database or listing of imported merchandise that would readily identify NAFTA transactions?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
19.	Does the importer or the importer's agent visit the plant in the NAFTA country where the goods are produced?					
20.	Does the importer perform an annual review of classification, specific rule changes affecting NAFTA?					
21.	Does management review the classification and eligibility of new NAFTA items?					
22.	Do contracts with NAFTA suppliers contain provisions to ensure compliance with NAFTA eligibility requirements?					
23.	Does the importer review entries to verify that correct classifications were used?					
24.	Does the importer verify that certificates of origin are on file for each entry of merchandise for which NAFTA preference is claimed?					

	Internal Control	Yes	No	Work Paper Reference		Comments
				IC Manual Page Number	Is Implementation of Control Supported by Documentation and/or Interviews?	
25.	Does the importer review NAFTA certificates of origin to ensure validity of the certificates?					
26.	Does the importer maintain entry documentation and associated NAFTA certificates of origin for 5 years after the date of importation?					
27.	Are HTSUS classifications for NAFTA merchandise maintained in a database that is provided to brokers?					
28.	Are brokers required to have written importer approval to making classification changes?					
29.	Does the importer provide adequate broker oversight?					
30.	List company-specific procedures below (if applicable)					

Section 2 - Preliminary Internal Control Assessment

Use information obtained in section 1 above to make a preliminary assessment of internal control as strong, adequate, weak, or nonexistent.

	Strong	Adequate	Weak	None*
Internal Control				

*If the team concludes that the company does not have internal control, risk is not acceptable so proceed to Section 5 below.

Section 3 – Sample Sizes

Use the matrix for determining Extensiveness of Audit Tests in section 3.3 of TIPS to determine the extensiveness of audit tests to confirm that internal control is effective. Multiple samples related to various costs comprising transaction value are possible. Samples and sample items should concentrate on risk.

Sample Area	PAR Level (High, Moderate, or Low)	Internal Control Level (Weak, Adequate, or Strong) From Section 2 Above	Testing Limit (1-20)

Section 4 - Results of Sample Testing

Use the results of sample testing to determine if internal control is effective.

Results of Testing	Yes or No
Is IC effective to provide reasonable assurance to preclude significant risk?	

Section 5 - Risk Opinion

Use the information developed in Sections 1-4 to record the PAS opinion that risk is acceptable or unacceptable.

Risk Opinion	Yes or No	
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		Comments
Acceptable		

If risk is not acceptable the audit team may need to proceed to ACT or have company do quantification.